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Interim Guidance Under §4960: Excise Taxes and Parachute Payments

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INTRODUCTION

Enacted on December 22, 2017, the 2017 tax act (Pub. L. No. 115-97, §13602(a)) added §4960 to the Internal Revenue Code.[1] This new section imposes an excise tax on the amount of ''remuneration'' in excess of $1 million, plus any ''excess parachute payment'' paid by an ''applicable tax-exempt organization'' to a ''covered employee.'' The excise tax is equal to the rate of tax under §11 (currently 21%).[2] Section 4960 applies to taxable years beginning after December 31, 2017.[3]

There is no grandfather relief for remuneration deferred before the adoption of §4960. Consequently, even tax-exempt organizations that do not routinely pay their senior executives over $1 million in annual compensation, as well as organizations with generous pre-existing severance benefits, can be subject to the excise tax. Moreover, §4960 applies to each ''applicable tax-exempt organization'' or ''ATEO,'' which is defined in a broad manner and captures organizations that may not traditionally be thought of as tax-exempt. For example, governmental entities that rely on §115(1) for the exemption from tax and political organizations under §527(e)(1) are included in the umbrella definition of ATEOs. Best practices will now require that tax-exempt organizations covered by the new rules track their covered employees even if there is only a remote possibility that they will be subject to tax.

To assist taxpayers, Notice 2019-09 (the Notice) provides interim guidance in Q&A format on the application of §4960. Pending the issuance of final regulations, the preamble to the Notice acknowledges that taxpayers may ''base their positions upon a good faith, reasonable interpretation of the statute, including consideration of the legislative history, if appropriate.'' The guidance provided by the Notice generally constitutes ''a good faith, reasonable interpretation of the statute.'' The Notice separately flags certain positions that ''the Treasury Department and the IRS have concluded are not consistent with a good faith, reasonable interpretation of the statutory language.'' These positions are identified and summarized in a table (Exhibit A).

The Notice anticipates the issuance of, and invites advance comments on, proposed regulations. Thus, stakeholders and other interested parties will have opportunities to provide input.

What follows is an overview of §4960, summary of the positions taken in the Notice, and discussion of whether such positions resolve patent ambiguities or represent interpretations that are aggressive (in our view) or likely to prove administratively daunting, troublesome, or costly to ATEOs, their boards, and management.

BACKGROUND

Under §4960(a), an ''applicable tax-exempt organization'' (ATEO) is liable for an excise tax at the rate specified in §11 (currently 21%) on:

(1) Any ''remuneration'' (other than an excess parachute payment) in excess of $1 million paid to

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[1] All section references are to the Internal Revenue Code of 1986, as amended (the Code), and the regulations thereunder, unless otherwise specified.

[2] §4960(a).

[3] Notice 2019-09, Preamble §K.

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a covered employee by an applicable tax-exempt organization for a taxable year, and

(2) Any ''excess parachute payment'' (as determined under §4960, which differs from the definition under §280G) paid by the ATEO to a covered employee.

Applicable Tax-Exempt Organizations

Section 4960(c)(1) defines the term ''applicable tax-exempt organization'' to mean any organization that for the taxable year:

(1) Is exempt from taxation under §501(a),

(2) Is a farmers' cooperative organization described in §521(b)(1),

(3) Has income excluded from taxation under §115(1), or

(4) Is a political organization described in §527(e)(1).

Organizations exempt from tax under §501(a) include organizations that are exempt under §501(c)(3) and §501(c)(4). The excise tax also applies to governmental entities exempt from tax under §115, and it would extend as well to ''dual-qualified organizations'' (governmental entities that are also recognized as tax-exempt under §501(c)(3)). Notably, there are governmental entities that rely on neither provision of the Code for their exemption from tax (e.g., a state, land-grant college that has not applied for tax-exempt status), which will escape the reach of §4960.

Covered Employees

Section 4960 applies to excess remuneration and excess parachute payments paid to ''covered employees.'' Section 4960(c)(2) defines the term ''covered employee'' to mean any employee (including any former employee) of an ATEO if the employee:

(1) Is one of the five highest compensated employees of the organization for the taxable year, or

(2) Was a covered employee of the organization (or any predecessor) for any preceding taxable year beginning after December 31, 2016.

The Notice clarifies that the common-law employer is generally liable for the tax, but when more than one related employer pays a covered employee either excess remuneration or an excess parachute payment, each employer is liable. The sole owner of the disregarded entity is treated as the common-law employer for these purposes. Subsequent Q&As establish rules for apportioning the liability among related employers. Importantly, a common-law employer may not avoid liability by reason of a third-party payor arrangement, e.g., payroll agent, common paymaster, professional employer organization, or any similar arrangement).[4] Rather, a payment to an employee by a third-party payor is considered paid by the common-law employer with respect to the services for which the payment is made.

Applicable Tax Year

Section 4960(a)(1) imposes a tax on ''so much of the remuneration paid (other than any excess parachute payment) by an applicable tax-exempt organization **for the taxable year** . . .'' (emphasis added). However, it is unclear whose (employee or employer) and which (calendar or fiscal) taxable year apply. The Notice clarifies that ''[e]xcess remuneration paid and excess parachute payments made in the calendar year ending with or within the taxable year of an ATEO or a related organization'' are treated as paid for that taxable year.[5]

THE TAX ON EXCESS REMUNERATION

Under §4960(a)(1), an ATEO is liable for an excise tax for any ''remuneration'' (other than an excess parachute payment) in excess of $1 million paid to a covered employee by an ATEO for a taxable year.

Remuneration; Payments by Related Organizations

Section 4960(c)(3)(A) defines the term ''remuneration'' to mean ''wages (as defined in section 3401(a)), except that such term shall not include any designated Roth contribution (as defined in section 402A(c)) and shall include amounts required to be included in gross income under section 457(f).''

Under §4960(c)(4)(A), remuneration paid to a covered employee includes remuneration paid by ''any related person or governmental entity.'' The term ''person'' for the purpose refers to the long-standing, presumably well-understood definition set out in §7701(a)(1) (an individual, a trust, estate, partnership, association, company, or corporation).

Section 4960(c)(4)(B) provides that a person or governmental entity is treated as ''related'' to an ATEO if such person or governmental entity —

(1) Controls, or is controlled by, the organization,

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[4] Notice 2019-09, Q&A 3.

[5] Notice 2019-09, Q&A 2.

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(2) Is controlled by one or more persons which control the organization,

(3) Is a supported organization (as defined in §509(f)(3)) during the taxable year with respect to the organization,

(4) Is a supporting organization described in §509(a)(3) during the taxable year with respect to the organization, or

(5) In the case of a voluntary employees' beneficiary association (described in §501(c)(9)), establishes, maintains, or makes contributions to such voluntary employees' beneficiary association.

As noted above, one of the keys to determining whether a person or entity is ''related'' is determining ''control.'' Section 4960 does not define what constitutes control for this purpose. The Notice does define control in the following situations:[6]

- **Stock corporation.** In the case of a stock corporation, control means ownership (by vote or value) of more than 50% of the stock in such corporation.
- **Partnership.** In the case of a partnership, control means ownership of more than 50% of the profits interest or capital interest in such partnership.
- **Trust.** In the case of a trust with beneficial interests, control means ownership of more than 50% of the beneficial interests in the trust.
- **Nonstock organization.** In the case of a nonprofit organization or other organization without owners or persons having beneficial interests (nonstock organization), including a governmental entity, control means that (i) more than 50% of the directors or trustees of the ATEO or nonstock organization are either representatives of, or are directly or indirectly controlled by, the other entity; or (ii) more than 50% of the directors or trustees of the nonstock organization are either representatives of, or are directly or indirectly controlled by, one or more persons that control the ATEO.[7]

Notably, these rules are significantly more restrictive than long-standing tax rules governing entities under common control in the private sector.[8] These rules are less restrictive than rules governing tax-exempt entities.[9]

Section 4960 is less clear on what control means in the case of a governmental entity. The Notice clarifies that governmental entities include ''organizations that have income excluded from taxation under section 115(1)'' and ''organizations that are exempt from taxation under section 501(a)'' (e.g., ''federal instrumentalities exempt from tax under section 501(c)(1) and public universities with IRS determination letters recognizing their tax-exempt status under section 501(c)(3)).''[10] The Notice helpfully reminds the reader that ''the income of a governmental unit generally is not taxable in the absence of specific statutory authorization for taxing that income.''[11] That is, not all governmental entities are described in or even covered by §115(1).[12] By way of example, a college or university that does not have a determination letter recognizing its exemption from taxation under §501(a)[13] and that does not exclude income from gross income under §115(1) is not an ATEO. Such a governmental unit may, however, be liable for excise tax under §4960 as a related organization.[14]

Lastly, the Notice clarifies that the constructive ownership rules of §318 relating to constructive ownership of stock or the principles of §318 (e.g., with regards to non-stock organizations) apply for purposes of determining control.[15]

Where the remuneration for more than one employer is taken into account, §4960(c)(4)(C) provides that liability for tax among such related employers is allocated ratably in proportion to the covered employee's remuneration paid by such employer.

Covered Employees

Section 4960(c)(2) defines the term ''covered employee'' to mean any employee (including any former employee) of an ATEO, if the employee is one of the ''five highest-compensated employees'' of the organization for the taxable year, or was a ''covered employee'' of the ATEO (or any predecessor) for any of the ATEO's preceding taxable years beginning after December 31, 2016.

The Notice provides that the determination of whether an employee is one of the five highest-compensated employees of an ATEO is made based

[6] Notice 2019-09, Q&A 8.

[7] Notice 2019-09, Q&A 8.

[8] *E.g.,* §414(b), §414(c).

[9] *E.g.,* Reg. §1.414(c)-5.

[10] Notice 2019-09, Q&A 5.

[11] *Id.*

[12] Notice 2019-09, Q&A 5. *See* Rev. Rul. 77-261 (noting that exclusion from income under §115(1) applies only to income accruing ''to a State or political subdivision therefor **derived from the exercise of an essential governmental function or from a public utility**'') (emphasis added).

[13] *But see* Notice 2019-09, Q&A 6 (explaining the a governmental entity that has a determination letter recognizing its tax exemption may relinquish the exemption and thereby no longer be a ATEO).

[14] Notice 2019-09, Q&A 5.

[15] Notice 2019-09, Q&A 8.

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on his or her remuneration ''for services performed as an employee of the ATEO, including remuneration for services performed as an employee of a related organization with respect to the ATEO.''[16] The remuneration used for this purpose is the remuneration paid to an employee during the calendar year ending with or within the ATEO's or related organization's taxable year. Remuneration paid for medical services (or veterinary services) is not considered for purposes of identifying the five highest-compensated employees, however.[17]

Whether an employee is one of the five highest-compensated employees ''is determined separately for each ATEO, and not for the entire group of related organizations.''[18] Consequently, each ATEO has its own five highest-compensated employees. The preamble defends this interpretation by analogy to the rules limiting the deduction allowed to publicly held corporations for compensation paid to certain senior executives and other highly paid employees.[19] The Notice observes that Treas. Reg. §1.162-27(c)(1)(ii) treats publicly held corporations and all nonpublic corporations related to the publicly held corporation as a single corporation, but that §4960 does not do so. (One wonders why the Service could not simply adopt a parallel rule in a final §4960 regulation.) Accordingly the Notice provides that the position that ''a group of related organizations with more than one ATEO has a single set of five highest-compensated employees is not consistent with a good faith, reasonable interpretation of section 4960.''[20]

Helpfully, the Notice provides a limited service exception by providing that an employee is not treated as one of an ATEO's five highest-compensated employees for a taxable year if, during the calendar year ending with or within the taxable year, the ATEO paid less than 10% of the employee's total remuneration. This rule does not apply, however, if no ATEO in the group paid at least 10% of the employee's total remuneration for the year.[21]

Excess Remuneration

Section 4960(c)(3) defines ''remuneration'' with reference to §3401(a) (wages), except that it excludes any designated Roth contribution (as defined in §402A(c)) and includes amounts required to be included in gross income under §457(f). Remuneration includes an amount that is a parachute payment; however, a parachute payment is not subject to tax as excess remuneration if it is also subject to tax as an excess parachute payment under §4960.[22] Thus, remuneration is not subject to tax as both excess remuneration and as an excess parachute payment.[23] Remuneration includes remuneration paid to a covered employee by any related organization with respect to the employee's employment by such related organization.[24]

Compliance with §4960 requires an ATEO to determine the year in which remuneration is paid. The general rule, articulated in §4960(a) (flush language) is that remuneration is ''treated as paid when there is no substantial risk of forfeiture (within the meaning of section 457(f)(3)(B)) of the rights to such remuneration.'' As noted above, however, §4960(c)(3)(A) provides that remuneration generally means ''wages'' within the meaning of §3401. There is a latent ambiguity here: Prop. Reg. §1.457-12(e)(1), adopts the short-term deferral rule[25] for deferrals of compensation that would otherwise be subject to §457(f). Where the short-term deferral rule applies, a payment that would otherwise be taxed on vesting in one year will instead, if timely paid, be taxed, and constitute wages, in the following year. The Notice clarifies that short-term deferrals are treated as remuneration in the year in which paid—the year in which the remuneration is treated as wages.[26] Thus, the cross-reference to §3401 is not a timing rule; rather it merely establishes the scope of the term ''remuneration.''[27]

Medical and Veterinary Services

Section 4960(c)(3)(B) and §4960(c)(5)(C)(iii) exclude from remuneration and parachute payments, respectively, amounts paid to a licensed medical professional (including veterinarian) for the performance of medical or veterinary services.

The Notice clarifies that a licensed medical professional is a person licensed under state or local law to perform medical or veterinary services.[28] This would generally include dentists and nurse practitioners and may include other medical professionals depending on state or local law.

The Notice reads the term ''medical services'' narrowly for purposes of determining whether services

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[16] Notice 2019-09, Q&A 10(a).

[17] *Id.*

[18] Notice 2019-09, Preamble §C.

[19] *See* §162(m)(1) - §162(m)(4).

[20] Notice 2019-09, Preamble §C.

[21] Notice 2019-09, Q&A 10(b).

[22] Notice 2019-09, Q&A 12.

[23] *See id. See also* §4960(a)(1).

[24] Notice 2019-09, Q&A 12(c).

[25] Reg. §1.409A-1(b)(2). *See also*, Brian Gallagher, *Section 4960: Unpleasant Surprises and Unanswered Questions for Tax-Exempt Entities with 457 Plans*, The Tax Lawyer, Vol. 72, No. 1, pp. 223 et seq. (Fall 2018).

[26] *See* Notice 2019-09, Q&A 13.

[27] Notice 2019-09, Preamble §D.

[28] Notice 2019-09, Q&A 15(b).

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are medical services. The Notice relies on the definition of medical care under §213(d), which provides that medical services consist of services for the ''diagnosis, cure, mitigation, treatment, or prevention of disease, or for the purpose of affecting any structure or function of the body.''[29] For a veterinarian or other licensed veterinary professional, this standard is applied by analogy to determine whether the activity constitutes veterinary services.[30] Thus, activities related to medical services, such as administrative, teaching, and research services, are **not** medical services under this standard. The Preamble to the Notice helpfully points out, however, that ''to the extent a licensed medical professional provides direct medical care to a patient in the course of these activities, he or she performs medical services.''[31]

When a covered employee is compensated for both medical services and other services, the employer must make a reasonable, good faith allocation of remuneration paid to such employee between medical services and such other services. For example, the Notice provides that taxpayers may rely on a reasonable allocation set forth in an employment agreement that explicitly allocates a portion of the remuneration as for medical services or other services. But if the allocation set out in an employment agreement is not reasonable, taxpayers are admonished to use a reasonable method of allocation. The Notice offers as an example of a reasonable method, the use of ''records such as patient, insurance, and Medicare/Medicaid billing records or internal time reporting mechanisms to determine the time spent providing medical services.[32]

THE TAX ON EXCESS PARACHUTE PAYMENTS

Under §4960(a)(2), an ATEO is liable for an excise tax for any ''excess parachute payment'' paid by the ATEO to a covered employee. As some practitioners may notice, the excess parachute payment rules under §4960 are modeled after the rules set forth in §280G.[33]

The Notice summarizes the basic steps to determine the amount of excise tax (if any) under §4960(a)(2):

(1) Determine if a covered employee is entitled to receive payments in the nature of compensation that are contingent on an involuntary separation from employment and are not subject to an exclusion.

(2) Calculate the total aggregate present value of the contingent payments, taking into account the special valuation rules that apply when an involuntary separation from employment accelerates payment or vesting of a right to a payment.

(3) Calculate the covered employee's base amount with respect to the base period.

(4) Determine if the contingent payments are parachute payments. The contingent payments are parachute payments if their total aggregate present value equals or exceeds an amount equal to three times the covered employee's base amount.

(5) Calculate the amount of excess parachute payments. A parachute payment is an excess parachute payment to the extent the payment exceeds the base amount allocated to the payment. This is the excess over one times the base amount, and not the excess over three times the base amount.

(6) Calculate the amount of excise tax under §4960(a)(2).[34]

Excess Parachute Payments

Section 4960(c)(5)(A) defines the term ''excess parachute payment'' to mean ''an amount equal to the excess of any parachute payment over the portion of the base amount allocated to such payment.'' Further, §4960(c)(5)(B) defines the term ''parachute payment'' to means any payment ''in the nature of compensation'' to (or for the benefit of) a covered employee if—

(1) Such payment is contingent on such employee's separation from employment with the employer, and

(2) The aggregate present value of the payments in the nature of compensation to (or for the benefit of) such individual which are contingent on such separation equals or exceeds an amount equal to three times the base amount.

Section 4960(c)(5)(C) excludes the from this definition of a parachute payments: (1) payments from

[29] Notice 2019-09, Q&A 15(c) (referencing §213(d)(1)(A)).

[30] Notice 2019-09, Q&A 15(c).

[31] Notice 2019-09, Preamble §E.

[32] Notice 2019-09, Q&A 15(d).

[33] *See* §280G. Section 280G denies a tax deduction to corporations for ''parachute payments'' made to ''disqualified individuals'' that exceed a specified amount. Correspondingly, §4999 imposes a nondeductible 20% excise tax, over and above regular income tax, on recipients of excess parachute payments. Under §280G, parachute payments means payments: (1) in the nature of compensation to a ''disqualified individual''; (2) that are contingent on a change in control; and (3) where the aggregate present value equals or exceeds three times a base amount defined under §280G(b)(3). Disqualified individuals are employees, contractors, or other service providers who are also either officers, highly compensated individuals, or significant shareholders.

[34] Notice 2019-09, Preamble §F.

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qualified plans (including 403(b) plans);[35] (2) payments ''to a licensed medical professional (including a veterinarian) to the extent that such payment is for the performance of medical or veterinary services by such professional,''(3) and payments to individuals who are not ''highly compensated employees'' as defined in §414(q). Payments from an eligible deferred compensation plan (a §457(b) plan) maintained by a tax-exempt employer that is not a state or local government are **not** excluded.

Importantly, a payment is contingent on a separation from employment if the payment would not have been made in the absence of an involuntary separation from employment.[36] An involuntary separation from employment means any ''separation from employment due to the independent exercise of the employer's unilateral authority to terminate the employee's services, other than due to the employee's implicit or explicit request, if the employee was willing and able to continue performing services.''[37] If the right to a payment vests as a result of an involuntary separation from employment, the payment is treated as a payment that is contingent on a separation from employment. Thus, severance payments provided under employment agreement that vest upon an involuntary separation from employment are payments contingent on a separation from employment.[38] But not all payments that are made after an involuntary separation from employment are contingent on a separation from employment, e.g., a payment of previously vested deferred compensation that is paid on an involuntary separation from employment, or excess remuneration that was treated as paid before separation from employment.[39]

The Notice generally adopts the standards of the final §409A regulations for purposes of determining whether there has been a separation from employment, except that a bona fide change from employee to independent contractor status is treated as a separation from employment.[40] For purposes of §4960, an anticipated reduction in the level of services of more than 80% is treated as a separation from employment and an anticipated reduction in the level of services of less than 50% is not treated as a separation from employment, with the treatment of an anticipated reduction between these two levels depending on the facts and circumstances.[41]

Subject to an anti-abuse rule, if a payment is accelerated or a substantial risk of forfeiture lapses as a result of an involuntary separation from employment, the additional value due to the acceleration is treated as a payment contingent on a separation from employment.[42] This rule is based on Reg. §1.280G-1, Q&A 24(b) and (c).

Three-Times-Base-Amount Test for Parachute Payments/Computation of Excess Parachute Payments

To determine whether payments made to a covered employee separating from employment are parachute payments, the payments must be compared to the individual's ''base amount.'' This requires the ATEO or related organization to determine whether the aggregate present value (determined as of the date of the separation from employment) of all such payments are contingent on the separation.[43] For this purpose, the present value is determined applying a discount rate equal to 120% of the applicable federal rate.[44] If this aggregate present value equals or exceeds the amount equal to three times the individual's base amount, the payments are parachute payments.[45] The Notice provides rules for determining parachute payments where a covered employee is compensated by more than one, related organization.[46]

Section 4960(c)(5)(D) defines ''base amount'' by reference to rules ''similar'' to §280G(b)(3), which defines the ''base amount'' as the individual's annualized includible compensation for a ''base period.'' For purposes of §4960, the base period is the covered employee's five most recent taxable years ending before the date on which the separation from employment occurs. But if the covered employee was not an employee of the ATEO for this entire five-year period, the individual's base period is the portion of the five-year period during which the covered employee performed services for the ATEO, a predecessor entity, or a related organization.[47]

EXAMPLE: Assume a departing executive has been paid $125,000 per year for the past five years

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[35] §4960(c)(5)(C)(i), §4960(c)(5)(C)(ii). Qualified plans include a simplified employee pension plan, a simple retirement account, a tax-deferred annuity, or an eligible deferred compensation plan of a state or local government employer.

[36] Notice 2019-09, Q&A 20(c).

[37] Notice 2019-09, Q&A 22.

[38] Notice 2019-09, Preamble §F.

[39] Notice 2019-09, Q&A 20.

[40] Notice 2019-09, Q&A 23.

[41] Reg. §1.409A-1(h)(1)(ii). The Notice does not adopt the rule that permits an employer to modify the level of the anticipated reduction in future services that will be considered to result in a separation from employment.

[42] Notice 2019-09, Q&A 24.

[43] *See* Notice 2019-09, Q&A 25 and 26.

[44] Notice 2019-09, Q&A 27.

[45] Notice 2019-09, Q&A 25.

[46] Notice 2019-09, Q&A 33.

[47] Notice 2019-09, Q&A 30.

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(the base period). She commences to receive a promised 15-year term certain annuity (with no refund features) under an arrangement that is governed by §457(f). The annuity pays in annual installments of $100,000. Assume further that, as of the date of the executive's separation from employment, a reasonable discount rate is 3.5%.[48] The present value of the annuity is $,151,741, which is greater than three times the base amount (3 x $125,000 = $375,000). $776,741 ($1,151,741 - $375,000) is a parachute payment, the tax on which under §4960(a)(2) equals $163,115.61.

REPORTING

Taxes imposed under §4960 are reported and paid using Form 4720, Return of Certain Excise Taxes Under Chapters 41 and 42 of the Internal Revenue Code. Where remuneration is paid by an ATEO and one or more related organizations, each ATEO and related organization (including a related taxable organization) must file a separate Form 4720 to report its share of liability.[49] Taxes imposed under §4960 are paid and reported by filing Form 4720 by the 15th day of the fifth month after the end of the employer's taxable year. An employer may file Form 8868, Application for Automatic Extension of Time to File an Exempt Organization Return, to request an automatic extension of time to file.[50]

CONCLUSION

From the perspective of the board or management of an ATEO, there is a lot not to like in §4960 and the IRS's interpretation of the statute in the Notice.

The Conference Committee Report[51] accompanying the 2017 tax act explains the reasons for adding §4960, which include a solicitousness for an ATEO's principal purposes; the belief that excessive compensation ''diverts resources from those particular purposes;'' and to make the ''system fairer for all businesses.'' These rationalizations are less than compelling our view. The compensation paid by ATEOs, particularly large ATEOs, is driven by the market and constrained by long-standing rules governing intermediate sanctions.[52]

ATEOs will, of course, do their best to limit their exposure to §4960 by proper planning. For example, some ATEOs have already swapped unvested benefits under ineligible plans of deferred compensation covering senior executives for split dollar arrangements. But it's a safe bet that many ATEOs will simply choose to pay the tax, with the unavoidable and unfortunate result of diverting money from the ATEOs primary purposes. Thus, the new rule could produce an outcome entirely at odds with Congressional intent.

The notion that the adoption of §4960 will put all businesses—for profit and tax-exempt alike—on an equal footing is similarly odd. Executives of tax-exempts are ineligible for all manner of equity-based compensation widely available to their counterparts in private sector companies. It's hard to see how §4960 somehow levels a proverbial uneven playing field. If anything, tax-exempt employers appear to be marginally worse off.

Lastly, we find disturbing the lack of any grandfather provisions exempting remuneration paid before the enactment of the 2017 tax act. Compensation that may in many instances have accrued over many years is now being subject to a different and more costly and burdensome set of rules. This omission cries out for a (not-so) technical correction.

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[48] Rev. Rul. 2019-4.

[49] Notice 2019-09, Q&A 33.

[50] Notice 2019-09, Q&A 34.

[51] H.R. Rep. No. 115-466, at 494 (2017).

[52] §4958; Reg. §53.4958-1 *et seq*.

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EXHIBIT A

Notice 2019-09

Table of Positions Deemed to Be Inconsistent with "A Good Faith, Reasonable Interpretation of the Statutory Language"

The Preamble to Notice 2019-09 provides that:

> "Until further guidance is issued, to comply with the requirements of section 4960, taxpayers may base their positions upon a good faith, reasonable interpretation of the statute, including consideration of the legislative history, if appropriate. The positions reflected in this notice constitute a good faith, reasonable interpretation of the statute. Whether a taxpayer's position that is inconsistent with this notice constitutes a good faith, reasonable interpretation of the statute generally will be determined based upon all of the relevant facts and circumstances, including whether the taxpayer has applied the position consistently and the extent to which the taxpayer has resolved interpretive issues based on consistent principles and in a consistent manner. **Notwithstanding the previous sentence, this preamble describes certain positions that the Treasury Department and the IRS have concluded are not consistent with a good faith, reasonable interpretation of the statutory language.** The Treasury Department and the IRS intend to embody these positions as part of the forthcoming proposed regulations."

The following is a summary of positions in the Notice that are "not consistent with a good faith, reasonable interpretation" of §4960:

Item No.	Statutory Requirement	Requests from Commentor(s)	Positions that are "not consistent with a good faith, reasonable interpretation of the statutory language"
(1)	Section 4960(c)(4)(B) defines "related organizations" to apply to any "person or governmental entity" that meets any of the relationship tests in §4960(c)(4)(B)(i)-(v).	A commenter requested guidance providing that remuneration paid by a separate employer that is a related for-profit or governmental entity (other than an ATEO) is taken into account in determining whether a covered employee has remuneration in excess of $1 million, but that the related entity is **not** liable for its share of the excise tax under §4960. The IRS rejected this approach noting that "[t]here is no statutory support for creating such an exception for for-profit and governmental entities."[53]	The position that a for-profit or governmental entity that is a related organization with regard to an ATEO is not liable for its share of the excise tax under §4960 is not consistent with a good faith, reasonable interpretation of the statute.
(2)	Section 4960(c)(2) defines a covered employee as any employee who is one of an ATEO's five highest-compensated employees for the current taxable year or who was a covered employee of the ATEO (or any predecessor) for any preceding taxable year beginning after December 31, 2016.	Commentors requested a rule of administrative convenience under which a covered employee is no longer considered a covered employee of an ATEO after a certain period of time. The IRS's position is that such rule would be inconsistent with the statute.[54]	The position that a covered employee ceases to be a covered employee after a certain period of time is not consistent with a good faith, reasonable interpretation of the statute.
(3)	Section 4960(c)(3)(B) excludes from the definition of remuneration, amounts paid to paid for medical services.	A commenter proposed that remuneration paid for medical services be taken into account for purposes of determining the five highest-compensated employees.[55]	The Notice determines that: "An interpretation that remuneration for medical services is taken into account for purposes of identifying the five-highest compensated employees would be inconsistent with the statutory structure and the legislative intent." Such a position is not consistent with a good faith, reasonable interpretation of §4960.
(4)	Section 4960(c)(2) defines the term "covered employee" to mean an employee is one of the five highest-compensated employees.	Commenters suggested that "a group of related ATEOs should have only five highest-compensated employees among all of the related ATEOs."	Noting that §4960 does not contain provisions that parallel Reg. §1.162-27(c)(1)(ii) (which treats a publicly held corporation and all nonpublic corporations related to the publicly held corporation as a single corporation), the Notice concludes that the position that a group of related organizations with more than one ATEO has a single set of five highest-compensated employees is not consistent with a good faith, reasonable interpretation of §4960.[56]

[53] Notice 2019-09, Preamble §A.
[54] Notice 2019-09, Preamble §C.
[55] Notice 2019-09, Preamble §C.
[56] Notice 2019-09, Preamble §C.

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